CHAPTER VII INVESTMENT CLIMATE

A. Government Attitude Toward Foreign Investment

A.1. Openness To Foreign Investment:

Japan, the world's second-largest economy, is an immense potential market for U.S. foreign direct investment (FDI). The Government of Japan (GOJ) imposes few formal restrictions on FDI in Japan, and has removed or liberalized most legal restrictions that apply to specific economic sectors. The government does not impose export-balancing requirements or other trade-related FDI measures on firms seeking to invest in Japan. Moreover, risks associated with investment in many other countries, such as expropriation and nationalization, are not an issue in Japan.

Despite Japan's attractive characteristics as a potential investment site, FDI levels have remained small relative to the size of the economy, reflecting a range of long-standing structural impediments. The challenges facing foreign investors seeking to establish or enhance their presence in Japan -- many of the most important of which are matters of private business practice rather than of government regulation -- include:

--A high overall cost structure that makes market entry and expansion expensive;

--Corporate practices and market rules that inhibit foreign acquisition of Japanese firms, such as insufficient financial disclosure practices, cross-holding of shares among keiretsu member firms, and the low proportion of publicly traded common stock relative to total capital in many companies;

--Exclusive buyer-supplier networks and alliances, still maintained by some Japanese companies belonging to the same business grouping (or "keiretsu"), which limit competition from foreign firms and domestic newcomers;

--Laws and regulations that directly or indirectly restrict the establishment of business facilities and hinder market access for foreign products, services, and FDI; and

--Close ties between government and industry, as illustrated by the delegation of quasi-regulatory authority to trade associations, which are often allowed to devise their own rules to regulate their business sectors.

These and other obstacles make Japan's investment environment relatively costly and difficult to navigate. In JFY 1999, Japan's annual inward FDI totaled $21 billion, or only about 0.5% of GDP. Although the JFY 1999 statistics showed a dramatic improvement on previous years' performance, Japan continues to host the smallest amount of inward foreign investment as a proportion of total output of any major OECD nation. Foreign participation in mergers and acquisitions (M&A), which account for some 80% of FDI in other OECD countries, although on an upward trend, also lags in Japan. Meanwhile, Japan continues to run a substantial imbalance between its inward and overseas FDI (see Table 1). In JFY 1999, a year of record-high inward investment flows, Japan reportedly invested over $66 billion overseas, while attracting only about one-third of that amount in inward direct investment. Japan's relative lack of foreign investment also acts as a restraint on the expansion of imports.

The most extensive changes, and much of the recent FDI flows, have come in the financial services sector. The 1995 Financial Services Agreement began a process of comprehensive liberalization which culminated in the "Big Bang." In the past two years, ongoing economic restructuring (due in large part to the more competitive financial sector and greater emphasis on rate of return), and changes in Japan's financial markets contributed to growth in foreign direct investment in Japan in non-financial sectors. At the same time, structural impediments to foreign investment remain, and it is not certain that inward foreign investment flows will continue to accelerate. Over the past two years, distribution affiliations, joint ventures, and mergers and acquisitions involving foreign and Japanese financial services providers have accelerated rapidly. As foreign firms take advantage of business opportunities being created in Japan's financial sector as a result of the Japanese government's "Big Bang" deregulation initiative, Japanese financial firms have started to look overseas for assistance in the form of new products, technologies and capital to meet these challenges. In addition, foreign firms have stepped in to buy the assets of domestic financial services firms that have recently failed.

Acknowledging that FDI in Japan lags far behind that of other industrialized economies, the GOJ has in recent years taken some welcome steps to address investment-related problems. In 1994, the GOJ established the Japan Investment Council (JIC), chaired by the Prime Minister, and started cabinet-level discussions on ways to improve Japan's investment climate. Since then, the JIC and other GOJ advisory groups -- such as the Prime Minister's Economic Council and various deregulation and administrative reform committees -- have issued statements calling for stronger government efforts to promote FDI as a means of ensuring long-term growth and vitality in key industrial sectors.

Most recently, in April 1999, the JIC issued a report incorporating seven sets of recommendations for improving Japan's investment environment, and the Prime Minister released an official policy statement noting that increased foreign investment is vital to the reinvigoration of the Japanese economy. Generally speaking, there are strong indications that the Ministry of International Trade and Industry (MITI) in particular is taking seriously the challenge of attracting greater foreign investment to Japan. At the regional level, a number of prefectural and city governments are intensifying their efforts to attract foreign investors, although they are hampered by limited financial resources.

Liberalization of Investment Restrictions: Japan has gradually eliminated most of the formal restrictions governing its FDI regime. In 1991, the GOJ amended the Foreign Exchange and Foreign Trade Control Law (which also controls foreign investment) to replace the long-standing "prior notification" requirement for all FDI with an "ex post facto notification" requirement for investment in non-restricted industries. "Prior notification" (and thus case-by-case approval) is now required only for investment in certain restricted sectors, including agriculture, forestry, petroleum, electrical/gas/water utilities, aerospace, telecommunications, and leather manufacturing (see the Appendix for a full list of reserved sectors). It is widely understood that administrative approval for foreign investment in some of these sectors is quite certain, while in other sectors it is likely to be discouraged, if the government finds that the investment would "seriously and adversely affect the smooth performance of the national economy."

U.S. investment has become increasingly common in some restricted sectors, particularly in the petroleum and telecommunications industries, although the criteria for defining and controlling these areas are unclear and could potentially inhibit further investment depending on the Japanese political environment. In February 1998, the Telecommunications Business Law and the Radio Law were amended and all restrictions on foreign ownership were removed with respect to Type I telecommunications carriers including their radio stations (with the exception of NTT and KDD). Further, restrictions on foreign ownership in KDD were abolished in July 1998. The Cable Television Broadcast Law was revised to remove foreign ownership restrictions on cable television companies in June 1999.

Several sections of the Japanese Antimonopoly Law (AML) are relevant to FDI. For example, chapter four of the AML includes extensive antitrust provisions pertaining to international contract notification (section 6), stockholding (section 10, 14), interlocking corporate directorates (section 13), mergers (section 15), and acquisitions (section 16). The stated purpose of these sections is to restrict any stockholding, management, joint venture, and M&A activities that constitute unreasonable restraints on competition or involve unfair trade practices. These provisions are not intended to discriminate against foreign companies or to discourage FDI.

Limitations on Facility Development, and Availability of Investment Real Estate: While the price of real estate has been falling for some years in Japan, particularly in the urban centers, potential foreign investors still point to high real estate-related expenses and regulations as obstacles to investment in Japan. Urban land remains expensive, and the rate of property turn-over is slow enough that investors frequently have trouble assembling property of sufficient size to accommodate their operations. A shortage of information on land prices and ownership also impedes foreign and domestic investors, by making it harder to assess the real asset value of potential business partners or acquisition targets; it also inhibits faster development of the domestic market for estate-related financial products.

A law to stimulate Japan’s rental property market by introducing a fixed-term lease system took effect in March, 2000. Under the new law, property owners can terminate leases upon expiration of the contract, making it easier for them to evict tenants and to project rental income. Previous law strongly favored tenants, who could refuse to move even after their lease expired. Revisions to the Securities Investment Trust Law, which were enacted at the same time, lifted the ban on real estate investment trusts (REITs). The revised law permits marketing of mutual funds that invest in property rights. These revisions are expected to encourage development of residential property while diversifying financial products.

In January, 2000, the Japan Institute of Certified Public Accountants introduced a standard requiring companies to write off unrealized losses on real estate inventories acquired for sale or development, further encouraging liquidity in real estate markets.

Japan continues to restrict the development of industrial and commercial facilities in some areas in an attempt to prevent excessive concentration of development in the environs of Tokyo, Osaka, and Nagoya, and also to protect land designated as optimal for agriculture. On the other hand, many prefectural governments outside the largest urban areas will make available property in public industrial parks. Generally speaking, Japan's zoning laws give local Japanese officials and residents considerable discretionary authority to screen almost all aspects of a proposed building. These factors effectively reduce the real estate available for development and often lead to delays in construction and higher building costs.

The Large-scale Retail Store Law (LRSL), designed in part to protect local merchants from large retail competition, continues to challenge foreign investors by limiting the establishment, expansion, and business operations of large Japanese stores, which are most likely to serve as distributors of imported products. The Law was eliminated June 1, 2000, and is being replaced by a new store location law, which emphasizes the preservation of the living environment rather than the protection of small business. Both foreign and domestic large retailers, however, continue to anticipate that they will experience difficulty establishing retail facilities under the new, locally-administered rules.

In February 1997, the Japanese Cabinet tasked the government to study ways of improving the quality and availability of public information on land price, transaction, use, and ownership. Also, incentive measures have been introduced to relax floor area ratio restrictions for projects which provide new open-space or improve urban infrastructure. In September 1998, the National Land Use Planning Act was amended to replace the prior notification system of large-scale land transactions with an ex post facto notification system.

In December 1999, the Diet approved the Law concerning Special Measures for Encouragement of the Supply of Quality Rental Housing and Other Facilities, which was designed to introduce a fixed-term housing leasehold system. The bill went into effect on March 1, 2000. Under this bill, housing lease relationships could be set to definitely terminate with the expiration of the stipulated contract period.

Aiming to increase the liquidity of Japanese real estate markets, over the past four years the government has progressively lowered capital gains, registration, and license taxes on real estate. Starting in 1998, the national Land Value Tax on property holding was suspended, although local property taxes remain considerable.

Corporate Tax Treatment: Local branches of foreign firms are generally taxed only on corporate income derived from within Japan, whereas domestic Japanese corporations are taxed on their worldwide income. Calculation of taxable income and allowable deductions, and payments of the consumption tax (sales tax), are otherwise the same as those for domestic companies, with national treatment for foreign firms. Corporate tax rules classify corporations as either foreign or domestic depending on the location of the head office, without regard to the place of incorporation. The U.S.-Japan Tax Treaty provides for the avoidance of double taxation.

Dividends distributed by a domestic Japanese firm are subject to a 20 percent withholding tax; the U.S.-Japan Tax Treaty reduces this tax to 10 percent for American shareholders. Interest payable to a nonresident is normally subject to withholding of 15 percent, but the Tax Treaty reduces this to 10 percent, as long as the interest is not attributable to a locally incorporated company. Royalties and fees paid to a foreign licenser by a Japanese licensee are subject to normal withholding of 20 percent, reduced to 10 percent by the Tax Treaty. A special tax measure allows designated inward investors to carry over certain losses for tax purposes for ten years rather than for the normal five years. In JFY96, the scope of losses that qualify for this special measure was expanded.

As part of the JFY99 Tax Reform, Japan's effective corporate tax rate, including local taxes, was reduced from 46.36% to 40.87%.

The Japanese government is also examining the introduction of a consolidated taxation system (affiliated corporations and subsidiaries are currently taxed on an individual basis). The lack of consolidated taxation in the nation's tax code is perhaps the most important tax disincentive for venture capital-type M&A activity in Japan. (Because of non-consolidated taxation, the losses usually expected at a new or acquired venture subsidiary cannot be charged against the profits of the parent firm or holding company.) Some quarters of the Japanese government remain reluctant to switch to consolidated taxation, however, fearing a possible significant decline in incoming tax revenue, and the actual timing for the switch remains uncertain.

Investment Incentives: The government-owned Development Bank of Japan (DBJ) , formed by merging the Japan Development Bank and the Hokkaido-Tohoku Development Finance Corporation, offers foreign-affiliated firms various lending programs under which foreign-owned companies (companies whose foreign capital ratio is one-third or higher) are eligible for low interest, long-term loans for capital investment. The loan amount may be up to 60% of the total investment amount and the loan period can run as long as 30 years. Interest rates are roughly competitive with the private long-term prime rate. Similar low-interest loan programs for foreign firms have been established by the Okinawa and Hokkaido-Tohoku Development Finance Corporations as incentives to foreign firms investing in these regions.

The "Technopolis" project, sponsored by MITI, is available to both Japanese and foreign firms. Under this program, MITI and prefectural governments can provide various types of assistance (e.g., preferential depreciation and land taxes) to companies locating in areas designated for development as a technology-intensive zone. As of June 1997, there were 26 areas throughout Japan with the Technopolis designation.

The GOJ has made efforts to improve the dissemination of FDI-related information and to facilitate investment opportunities through various government support services. The DBJ supports foreign companies by supplying market information on Japan (general data on industries, market scale, distribution channels, etc.) and by serving as consultants on specific investment projects. In June 1993, the GOJ established a business information support firm, called the Foreign Investment in Japan Development Corporation (FIND), which (for a fee) advises foreign firms on the many challenges and opportunities of investing in Japan and facilitates meetings with potential investment partners. FIND also publishes annual statistics on FDI in Japan and maintains detailed reference aids on FDI, such as local-level FDI programs. In response to the Japan Investment Council's April 1996 pledge to, in principle, support mergers and acquisitions, FIND set up a special M&A promotion division. Japanese local governments have in recent years shown increasingly sharp interest in attracting foreign investors to their districts. Most prefectural governments now offer an array of investment incentives including direct subsidies, and assistance in the form of grants and loans for facilities construction, and aid in paying for worker training and even worker salaries. In international comparison, however, these incentives still appear small in scale. Typically, even if a potential investing firm meets all of a prefecture's various criteria, the maximum incentive it can hope to receive has a value of less than $10 million.

The local government investment promotion efforts are also hampered by the fact that the local government is usually in the position of setting rigid conditions to qualify for incentives (by law), and sitting back and waiting for firms to show up which meet those criteria. Local government investment incentives also tend to be one-time, not lasting, and with the exception of the national government-sponsored incentives for investment in depressed areas, not related to taxes. This is because Japanese prefectures, not in control of their own tax laws, are not in a position to change them or interpret them flexibly. A total of 19 Japanese prefectures and cities maintain official trade and investment promotion offices in the U.S.

In general, although the Japanese government's FDI promotion efforts are well-intended, many U.S. firms have often found that incentive programs are insufficient in scope to overcome other problems they face.

A.2. Conversion and Transfer Policies:

All foreign exchange transactions to and from Japan -- including transfers of profits and dividends, interest, royalties and fees, repatriation of capital, and repayment of principal -- are, in principle, freely permitted unless expressly prohibited. With the April 1998 revision of the Foreign Exchange Law, Japan moved to a ex-post notification system. This means that all foreign exchange transactions (unless specifically prohibited, including certain foreign direct investments, listed in the Appendix) no longer require prior notification or approval. In addition, the new law eliminated the authorized foreign exchange bank system, whereby foreign exchange transactions all had to go through certain registered banks. All other restrictions on methods of payment -- including netting of settlements -- were also removed, enhancing the ability of foreign and Japanese financial firms to offer a fuller range of services in Japan. This has led to lower foreign exchange transaction costs for non-financial firms as well.

A.3. Expropriation and Compensation:

In the post-war period, the GOJ has not expropriated or nationalized any enterprises, with the exception of the nationalization in 1998 of two large capital-deficient banks, and expropriation or nationalization of foreign investments is unlikely in the foreseeable future.

A.4. Dispute Settlement:

There have been no major bilateral investment disputes since 1990, and there are no outstanding expropriation or nationalization cases in Japan, and no cases of international binding arbitration of investment disputes between foreign investors and the GOJ since 1952. Japan is a member of the 1958 New York Convention on the recognition and enforcement of foreign arbitration awards. However, it has long been an inhospitable forum for international commercial arbitrations. Prior to the March 1996 revision of the GOJ's Deregulation Action Plan, arbitration proceedings were viewed as the exclusive province of Japanese lawyers, with only limited exceptions. As a result, all documents had to be translated into Japanese even though the contract and all negotiations were in English. In step with deregulation, foreign lawyers were permitted to represent parties in international arbitration proceedings in Japan starting in 1996.

There are no legal restrictions on access by foreign investors to Japanese lawyers. However, strict limitations on legal practice in Japan by foreign lawyers, a prohibition on Japanese lawyers joining foreign-based law firms, and the small number of Japanese lawyers capable of handling international business transactions all constrain the ability of foreign investors to obtain adequate legal advice on doing business in Japan. Foreign lawyers licensed in Japan under the 1986 Foreign Lawyers Law are still not allowed to advise foreign investors on many aspects of investing in Japan, since such advice is considered as practicing Japanese law. The unnecessarily restrictive provisions of Japanese law and the rigid enforcement of these restrictions by the Federation of Japanese Bar Associations (*Nichibenren*) deprive foreign investors of the opportunity to receive the optimal combination of legal advice that a system more in conformity with current standards of international legal practice would allow. Recent deregulatory changes by the GOJ are unlikely to remedy this situation.

Japan's civil courts enforce property and contractual rights, and the courts do not discriminate against foreign investors. However, they are sometimes ill-suited for litigation of investment and business disputes. As in many other countries, Japanese courts operate rather slowly. In addition, the courts lack contempt powers to compel a witness to testify or a party to comply with an injunction, and timely temporary restraining orders and preliminary injunctions are difficult to obtain. While filing fees for large civil cases were reduced in 1992, they are still based on the amount of the claim, rather than a flat fee. A lawyers usually requires an up-front payment before commencing a case; contingency fees, while not unknown, are not common. The losing party can delay execution of a judgment merely by appealing, and on most appeals to the high courts, additional witnesses and other evidence are allowed.

Courts do have power to encourage mediated settlements, and mainly due to the low number of lawyers in Japan, it is very common for companies to settle out of court. Following the 1997 Deregulation Action Plan, the number of new lawyers admitted each year increased from 700 to 800 in 1998, and 1000 in 1999. The Ministry of Justice, the lawyers' union, and the Supreme Court are considering proposals to raise the number to 1500 per year.

A new Product Liability Law became effective in July 1995, but to date there have been only a few court cases. However, many companies have modified their design and production processes, as well as provided more detailed instruction and product manuals, in an effort to limit potential liability. Many industry associations have formed product liability study groups to deal with the law.

A.5. Performance Requirements and Incentives:

Japan does not maintain a system of performance requirements. Japan also maintains no formal requirements for local management participation or local control in joint ventures or other forms of direct investment, except in restricted sectors.

A.6. Right to Private Ownership and Establishment:

Japan secures the right for foreign and domestic private enterprises to establish and own business enterprises and engage in all forms of remunerative activity.

A.7. Protection of Property Rights:

Protection of intellectual property rights is an integral part of every successful U.S. exporter's basic market strategy in Japan. It is necessary to file applications to register patents and trademarks in Japan to obtain protection, but prior patent filing in the United States can provide certain advantages if applications are filed promptly in Japan. A U.S. patent or trademark attorney can provide informal advice, but it is necessary to hire a Japanese lawyer or patent practitioner (benrishi) registered in Japan to prosecute the patent or trademark application. In conformity with international agreement, Japan maintains a non-formality principle for copyright registration -- i.e., registration is not a pre-condition to the establishment of copyright protection. However, the Agency of Cultural Affairs maintains a registry for such matters as date of first publication, date of creation of program works, and assignment of copyright. U.S. copyrights are recognized in Japan by international treaty. U.S.-produced semiconductor chip design-layouts are protected for ten years under a special law if they are registered with the Japanese “Industrial Property Cooperation Center”-- a Japanese government-backed public corporation.

Obtaining and protecting patent and trademark rights in Japan can be time-consuming and costly, although patent fees have recently been reduced considerably. While the process to safeguard such rights might seem prohibitive, lack of protection would permit competitors both in and outside of Japan to copy a product or production process. Even when intellectual property rights have been acquired, pirating of technology and designs can occur in Japan, as in other countries. Each company in a trading or licensing agreement should understand clearly what its rights and obligations are with respect to the intellectual property rights owned or acquired by the other. Such a clear understanding helps to create a good rapport based on mutual trust, thereby ensuring the success of the trading or licensing agreement.

Patents, Trademarks, Utility Models and Designs: Unlike U.S. patent law, patents are granted to the first to file an application for a particular invention, rather than to the first to invent. Although Japan accepts filings in English (to be followed by a Japanese translation), companies should ensure that translations of their applications are perfect, as significant negative ramifications may result from translation errors. Prompt filing in Japan is crucial because printed publication of a description of the invention anywhere in the world, or knowledge or use of the invention in Japan, prior to the filing date of the Japanese application, would preclude the grant of a patent on the application. Also, unlike the United States, where examination of patent applications is automatic, an applicant must request examination of his patent application in Japan within three years of filing. (Reduced from seven years to three years starting October 1, 2000.)

As is true in many countries, all patent applications are published 18 months after filing. If, during the examination, the Japanese Patent Office (JPO) finds no impediment to the grant of a patent for a particular invention, it publishes the patent application in the Patent Public Gazette a second time, including any changes that have been made during the examination. Under a recent amendment to the Patent Law, parties may contest the terms of a patent grant immediately after issuance by the Patent Office (for a period of up to six months), rather than prior to registration as had been the previous practice. The patent is granted and valid for 20 years from the date the application is filed.

It takes an average of 19 months, according to the latest JPO statistics in CY 98, in Japan from the request for examination of application to First Action (the government aims to shorten this to 12 months by 2000) -- compared to 18 months in the United States for the entire patent process. An applicant can request accelerated examination, and efforts by the Patent Office to make the documentation necessary for the preliminary research required to request accelerated examination available electronically are expected to lower the cost of such requests to the applicant. During the examination period, limited effective legal protection exists.

Japan's Trademark Law protects trademarks and service marks. As is the case with patent applications, a resident agent (usually a lawyer or patent agent) must prosecute the trademark application. And as with the processing of patent applications, Japan's trademark registration process can be slow. Any company planning on doing business in Japan should file for trademark registration as early as practicable. Japan is subject to Madrid Protocol effective March 14, 2000 and trademark registered at WIPO Secretariat will be protected among member countries.

Japan's Utility Model Law also allows registration of utility models, a form of minor patent with an 6-year term of protection, retroactive from the date of application since January 1994. A separate design law allows protection of designs, with a 15-year term of protection from the date registration was made.

Unfair Competition and Trade Secrets: The only protection available for a trademark in Japan prior to registration is under the Japanese Unfair Competition Prevention Law. Under this law, the owner of the mark must demonstrate that the mark is well-known in Japan and that consumers will be confused by the use of an identical or similar mark by the unauthorized user. In 1990, Japan enacted amendments to the law that provided some protection from theft of trade secrets, such as know-how, customer lists, sales manuals, and experimental data. The law, which was amended completely in 1993, also provides for injunctions against wrongful use, acquisition, or disclosure of a trade secret by any person who knew or should have known that the information in question was misappropriated. The judicial process, however, makes the enforcement of rights without loss of trade secrets difficult.

A.8. Regulatory System: Laws and Procedures:

Japan's economy remains relatively heavily regulated for a major industrial country, which tends to limit investment opportunities, raise costs for Japanese businesses and consumers, and hamper employment mobility and business formation. Meaningful deregulation will improve market efficiencies and reduce costs. Combined with stronger antitrust enforcement and administrative reforms to increase the transparency of regulatory regimes, deregulation will help reduce structural problems that impede the sale of foreign goods and services and discourage FDI. The Japanese government and the business community have repeatedly stated that deregulation is a high-priority issue, but opposition to many specific proposals from vested interests remains strong.

The Japanese government has issued a series of deregulation action plans, and has charted some noteworthy deregulation measures in housing, land zoning, financial services, employment services, distribution and freight forwarding. On the other hand, the government has made little concrete progress and either postponed or failed to adequately address important issues in many other areas, including transportation (deregulation of trucking), and legal services.

Under the Antimonopoly Law, the Japan Fair Trade Commission (JFTC) is authorized to screen certain notifiable international contracts--such as joint ventures involving foreigners--and to prohibit specific contracts that, in the JFTC's judgment, might cause unreasonable restraints on trade or involve the use of unfair trade practices. In June 1997, however, the JFTC abolished its contract notification system, under which any Japanese entrepreneur who enters into an international contract that was notifiable under JFTC rules was required to file with the commission within 30 days of concluding such an agreement. The JFTC has also abolished 33 antitrust-exempted cartels, with four other exempted cartels scheduled to be eliminated in future years, leaving three antitrust-exempted cartels operating in Japan.

The United States continues to hold bilateral working-level discussions in an effort to encourage the Japanese to promote deregulation, competition policy, and administrative reform measures that would increase imports and foreign direct investment into Japan. The reader should consult the National Trade Estimate Report on Foreign Trade Barriers, issued by the Office of the U.S. Trade Representative (USTR) on March 31, 2000, for a detailed description of Japan’s regulatory regime as it affects foreign firms (both exporters and investors).

A.9. Capital Markets and Portfolio Investment:

Japan maintains no formal restrictions on inward portfolio investment, and in fact foreign capital occupies an increasingly important place in Japanese capital markets. However, corporate practices such as cross-shareholding limit the percentage of shares in individual firms and in the overall market that foreign investors can actually purchase, while informal restrictions on management participation of foreign shareholders limit the attractiveness of Japan's equity market to foreign investors.

Environment for Mergers and Acquisitions: Stock market-based takeovers of listed firms via tender offer, as widely practiced in the United States and parts of Europe -- both friendly and hostile -- remain extremely rare in Japan. Japan’s famous aversion to M&A activity is starting to fade, accelerated by the unwinding of extensive corporate cross-shareholding brought about by implementation of improved accounting standards. Tender offers for listed firms may increase as newly-listed firms in the over-the-counter (OTC) market -- which are less likely to become predominantly "cross-held" -- increase. But viewed historically, of the roughly 400 foreign investment M&A transactions in Japan since 1991 (including divestitures of overseas firms held by Japanese), only five cases involved tender offers for companies listed in Japan. (Even this was an improvement over the previous two decades, which saw only one such case.) The "acceleration" of tender offer activity in the 1990's stems directly from the 1990 elimination of the prior-to-offer reporting requirement (which stipulated that the Finance Ministry be informed of any tender offer nine days before its announcement) and the extension of the tender offering period to 60 days.

Friendly transfer of wholly-owned and majority-owned subsidiaries is a more common form of M&A in Japan. Similarly, there are signs that owner-operated unlisted firms -- which traditionally would only sell out as a last resort before bankruptcy -- are becoming more amenable to acquisition by foreigners. Particularly in the more modern, more service-oriented sectors of the economy, purchase by foreigners is becoming less of a badge of shame than in years past.

Still, there remain a number of key factors limiting greater entry into the Japanese market through M&A with unlisted firms -- including tax policy, weak accounting and disclosure practices, Japan's underdeveloped OTC stock market (which if more developed would reduce the risks involved in M&A), lack of readily available information on firms that might be acquired, and the relative lack of a M&A "infrastructure" in the form of specialists skilled in making matches and structuring M&A deals.

The past year saw introduction of two new exchanges geared towards encouraging start-ups and venture capital investments. In December, 1999, the Tokyo Stock Exchange introduced “Mothers,” with less-stringent listing criteria for emerging companies. In April, 2000, TSE announced it would tighten listing requirements and screening procedures (requiring new companies to post a full year of earnings before being listed) to prevent firms with mob connections from listing on the exchange.

NASDAQ Japan, in partnership with the Osaka Stock Exchange, opened June 19, 2000, with eight listed companies. NASDAQ announced that listing requirements will be the same as for NASDAQ’s New York exchange. Although the new exchanges have relatively few listed firms, as yet, and suffer from lack of liquidity, analysts expect the exchanges to develop a healthy competition and provide needed capital for entrepreneurs.

Cross-shareholding and M&A: Potential foreign investors in Japan frequently point out that extensive cross-shareholding (mochiai) in Japan greatly complicates market-based merger and acquisition (M&A) transactions, and reduces the potential impact of shareholder-based corporate governance. Corporate governance practices which result in senior management emphasis on internal loyalties over shareholder return can also lead to premature rejection of M&A offers. At the same time, many market observers believe Japanese markets are undergoing a clear trend of unwinding of cross-shareholding, which has accelerated in recent years under the pressure of difficult corporate finances. At the same time, more corporations are hiring board members from outside the firm, and placing greater emphasis on shareholder value in their management practices.

To assist corporations in reducing the unfunded liabilities of corporate pension funds, the Japanese government implemented legislation on April 1, 2000, which allows corporations to transfer shareholdings to their related corporate pension funds. The pension funds will be able to properly execute shareholder rights on the transferred shares, and sell the shares if deemed in the best interests of the pension-holders. This legislation is expected to help accelerate the unwinding of cross-shareholdings.

In another useful innovation, the Diet approved amendments to the Commercial Code permitting creation of a stock swap system, through which one of the parties becomes a wholly-owned subsidiary company and the other a parent company, as well as a stock transfer system to establish a parent company. Special tax treatment will be implemented in conjunction with the creation of the stock exchange and the stock transfer system to allow deferment of taxes on capital gains on stocks at the time of exchange and transfer. To take advantage of these new rules, however, foreign investors must legally establish a Japanese subsidiary firm to act as the counterpart to the stock exchange/transfer.

Accounting and Disclosure: Accounting and disclosure standards are an extremely important element in assessing and improving any nation's environment for mergers and acquisitions. Before any merger or acquisition can take place, it is critical that the merging or purchasing corporations have the best possible information on which to make business decisions. However, recent implementation of "Big Bang" associated accounting changes in the past year have significantly improved Japan's accounting standards.

Aside from the lack of publicly available data on the accounts of unlisted Japanese companies, a situation which also exists in the United States, the greatest problem from the perspective of promoting foreign M&A had been the use of book-value accounting rather than mark-to-market accounting. Consolidated accounting is also critical to accurately pricing subsidiaries for sale or purchase. Fortunately for potential investors, the Japanese government is following a timetable for introduction of consolidated and mark-to-market accounting for listed firms:

Starting in JFY99, effective control standards and influence standards were introduced in place of conventional holding standards, expanding the range of subsidiary and affiliated companies included for the settlement of account. Consolidated disclosure of contingent liabilities, such as guarantees, began in April 1998.

Market-value accounting: Starting in JFY00, all marketable financial assets held for trading purposes must be recorded at market price, except for cross-shareholdings and other long-term securities holdings for which market-value accounting is deferred until JFY01.

Also starting in JFY00, companies are expected to disclose unfunded pension liabilities by valuing pension assets and liabilities at market price. However, companies may defer implementation of this decision until the following year.

These improvements leave unresolved the matter of reporting and disclosure by unlisted firms and financial institutions -- which is determined by the Ministry of Justice-administered Commercial Code, not the Ministry of Finance-administered Securities Law. However Financial Supervisory Agency guidelines do regulate unlisted financial institutions, including unlisted life insurance companies.

The greater focus on consolidated results and mark-to-market accounting is already having an impact and is encouraging unwinding of cross-held shares. Corporate restructuring is accelerating, and companies are rushing to reduce pension under-funding. Banks have stared disposing of low-yield assets (aided by the stock price rally at the end of JFY99). While the recent improvement in accounting standards and growth in M&A activity have been welcome, they have also exacerbated the shortage of accounting professionals.

Taxation and M&A: Another unresolved issue is the question of reconciliation of Japan's accounting and tax regimes. In the area of taxation, in addition to the lack of a consolidated taxation system (noted in section A.1 above), there is the problem of preferential tax treatment of initial public offerings. Under current regulations, if a company is sold in an M&A transaction before IPO listing, a 26% capital gains tax rate applies, whereas if the founding shareholder of a company "goes public" and then sells shares of the company into the market, a capital gains tax rate of only 13% applies (if the sale is within the first year after listing). Alternatively, after waiting one year, the entrepreneur can take advantage of an even lower tax rate of only 1% of gross transaction proceeds. These policies result in medium-sized Japanese owner-managed firms developing "IPO fever," with the anticipation of the windfall of OTC market listing -- even though it may or may not happen soon -- leading them to be reluctant to be acquired. (In one recent poll, 85% of questioned Japanese venture capitalists said they were aiming for OTC listing.) Acquisition, however, is more likely before listing than after listing -- when the stock is held more diffusely and the relative dormancy of Japanese capital markets combines with the difficulty of friendly or hostile acquisition by tender offer to make acquisition much more difficult. The Japanese government and Japan Securities Dealers Association are currently considering plans to amend this situation.

Bankruptcy Laws: Smooth and flexible bankruptcy procedures make it easier for a corporation and its assets to be acquired or merged in a "rescue" format, thereby preserving employment and protecting underlying corporate value. Legal proceedings for disposal of insolvent corporation in Japan were carried out in accordance with the Bankruptcy Law, the Composition Law, the Corporate Reorganization Law, and the Commercial Law (re-organization of a company, and special liquidation). The Japanese government recognizes that these laws need to be adjusted and proceedings reassessed from the viewpoint of the entire legal system concerning insolvency.

Accordingly, the Ministry of Justice conducted a review of Japanese insolvency laws, with an emphasis on reorganization–type disposition procedures covering small and medium-sized enterprises. To promote the rational and flexible rehabilitation of the business and economic activities of debtors in distress, the Law for Rehabilitation of Civil Affairs ("Civil Revitalization Law") was enacted and went into force in April 2000. This is a reconstruction-type bankruptcy law designed to replace the Composition Law. Its main features include improved protection of debtor assets prior to the start of rehabilitation procedures; easing of requirements for start of rehabilitation procedures; simplified and rational procedures for the examination and determination of liabilities; improved procedures for approval of rehabilitation plans; and the provision of measures for ensuring proper execution of rehabilitation plans.

Credit Markets: Domestic and foreign investors have free access to a variety of credit instruments at market rates. In general, foreign companies in Japan have not experienced significant difficulties in obtaining funding. Most foreign firms secure short-term credit by borrowing from Japanese commercial banks or one of the many (close to one hundred) foreign banks operating in Japan. Medium-term loans are available from commercial banks, as well as from trust banks and life insurance companies. Large foreign firms have tended to use foreign sources for long-term financial needs, although increasingly sophisticated derivatives products are becoming available to assist in hedging each foreign investors' perceived risk.

A.10. Political Violence:

In general, political violence is rare in Japan, and acts of political violence involving American business interests are virtually unknown. The media has played up rumors of right-wing groups harassing foreign firms that have acquired real estate associated with non-performing loans, but there does not appear to be much substance to these reports.

A.11. Corruption:

The penal code of Japan covers crimes of official corruption. An individual convicted under these statutes is subject, depending on the nature of the crime, to penal servitude ranging from one month to fifteen years, and possible fines up to three million yen or mandatory confiscation of the monetary equivalent of the bribe.

While corruption usually involves the exchange of moneys, the methods in which business is conducted in Japan can often lead to what some foreign Japan-watchers have described as "institutionalized corruption." For example, the web of close relationships between Japanese companies, politicians, government organizations, and universities has been said to foster an inwardly-cooperative business climate that is conducive to the awarding of contracts, positions, etc. within a tight circle of local players.

Amakudari is the practice whereby senior government officials retire into top positions in Japanese companies, usually in industries that they once regulated. These officials then function as in-house consultants on regulatory matters and as lobbyists to their former ministries and agencies. Amakudari individuals are particularly common in the financial, construction, transportation, and pharmaceutical industries -- which, not coincidentally, are traditionally heavily-regulated industries. Foreign companies usually do not enjoy such pipelines into the bureaucracy, and thus are somewhat disadvantaged in their ability to understand and deal with laws, regulations, and informal ministry guidance. This disadvantage has been ameliorated somewhat in recent years by the introduction of more-transparent administrative procedures.

While there have been some high profile exposures -- particularly over the past year -- of officials having either given or accepted bribes, the Japanese government has not had an aggressive record of criminal prosecution. Those prosecuted have generally received suspended sentences. In some cases, the government is in the dilemma of deciding how to handle past activities such as "wining and dining" which were commonplace at the time, but which are now more explicitly banned.

Following reform in 1993, numerous shareholder civil suits have been filed. Japanese law also provides for company directors to be found personally liable for the amount of the bribe, and some judgments have been rendered against company directors. This change may significantly impact the payment of bribes, as individuals are held personally liable without the shield of the company to protect them, although there is currently discussion within the ruling political party of new rules to make it harder to file shareholder derivative lawsuits.

Japan has also ratified the OECD Anti-Bribery Convention, which bans the bribing of government officials in countries outside Japan.

B. Bilateral Investment Agreements

The 1952 U.S.-Japan Treaty of Friendship, Commerce, and Navigation gives national treatment and most favored nation treatment to most U.S. investments in Japan.

U.S.-Japan Investment Arrangement: U.S. Government concerns regarding barriers to foreign investment in Japan continue to be addressed through bilateral discussions under the U.S.-Japan Economic Framework. In July 1995, the U.S. and Japan signed the "Policies and Measures Regarding Inward Direct Investment and Buyer-Supplier Relationships." This document codified inward investment-related policies and promotion programs the Japanese government had instituted up to that time, and detailed further actions the GOJ intends to take to promote FDI into Japan. Significant measures included GOJ pledges to:

Extend the 1992 "Inward Investment Law" and to make its private participation promotion (or minkatsu) programs, including low interest loans and tax incentives, available to foreign investors; (As noted above, this law has been extended and will remain in effect until May 2006.)

Earnestly expand efforts to inform foreign firms about existing FDI-related financial and tax incentives, and to broaden eligibility criteria and lending under these programs; and

Strengthen the FDI promotion roles of such organizations as the Japan Investment Council, Office of the Trade and Investment Ombudsman, the Japan External Trade Organization, and the Foreign Investment in Japan Development Corporation (FIND).

Since July 1995, the bilateral Investment Working Group has met formally six times to review implementation of the “Policies and Measures” and to discuss other issues concerning FDI and buyer-supplier relations. Recent meetings focused on measures to improve the M&A environment in Japan, increase real estate market liquidity, and improve labor mobility. Expert hearings were held on these three subjects in July 1998. In addition, the Working Group organized two public symposia on M&A-related issues, and one public symposium on ways to improve Japanese local government investment incentives.

1999 Joint Report: In May 1999, the Working Group issued a detailed Joint Report to President Clinton and Prime Minister Obuchi concerning improvements in the environment for foreign investment in Japan and the U.S. Through this report, both governments emphasized the usefulness of increasing foreign investment flows into Japan and stressed their willingness to examine measures identified as important to improving the environment for foreign direct investment. In the report, the Working Group concluded that considerable steps have been taken toward improving the environment for foreign direct investment in Japan, and that improvement in Japan’s environment for foreign direct investment is accelerating. At the same time, the Report noted that additional steps are both necessary and worthwhile. The Working Group met again in October 1999 and April 2000 to review progress.

2000 Investment Symposium: On March 1, 2000, the Ministry of International Trade and Industry of Japan, the U.S. Department of State and JETRO jointly hosted the “Investment-in-Japan 2000” in Tokyo, under the auspices of the U.S.-Japan Investment Working Group. The symposium brought together more than 30 leading experts on investment and business from the corporate, academic and government sectors of both nations. Before an audience of approximately six hundred people, these experts discussed in detail Japan’s current investment climate. While the panelists gave much credit for the growth in investment in-flows and regulatory reforms Japan has undertaken in recent years, the panelists shared their recommendations regarding further changes to Japan’s legislative, regulatory and tax systems which would facilitate investment for both Japanese and foreign firms.

C. OPIC And Other Investment Insurance Programs

OPIC insurance and finance programs are not available in Japan. Japan has been a member of the Multilateral Investment Guarantee Agency (MIGA) since it was established in 1988. Japan's capital subscription to the organization is the second largest among member countries, after the United States.

D. Labor

The Japanese labor market today suffers from demographic, macro-economic, and structural pressures, which are slowly but surely changing traditional Japanese employment practices. The regulatory philosophy which has formed Japan's post-war labor laws is also changing, although perhaps more slowly. Foreign investors seeking to hire highly qualified workers in Japan will welcome most of these changes.

Japanese employment practices have been said to rest on "three pillars:" lifetime employment, seniority-based wages, and enterprise unions. In fact, these three aspects of the Japanese labor market have always applied only to the larger firms, and today all three are rapidly eroding. Demographic pressures – fewer young workers and a rapidly aging labor force – as well as the need for structural changes in the Japanese economy are forcing most firms to abandon both lifetime employment guarantees and seniority-based wages. Although labor unions play an important role in the annual determination of wage increases throughout the economy, only 23% of Japanese workers are now union members. In firms with less than 100 employees, only 0.6% are unionized.

Investors should be aware of Japan's high wage structure. Workers earned an average of approximately 300,000 yen per month in base wages last year, with significant variations by education, age/seniority and position. Occupational wage differentials are much smaller than in most countries. However, the Japanese Federation of Employers estimates that base wages are only 58% of total wage costs. Annual summer and year-end bonuses add, on average, another 34%. Relatively high statutory welfare contributions are also required for basic government pensions, health and accident insurance, and unemployment insurance. Most companies also incur other employee welfare costs for family and/or transportation allowances, company-provided pension schemes, and such in-kind payments as housing for some employees. Off-setting these high wage costs, of course, is the fact that the Japanese work force is highly educated, disciplined, loyal to their employer, and motivated to assure the economic well-being of the company.

Japanese workers are classified as being either "regular" or "other" employees. Regular employees are usually recruited directly from schools or universities and given an employment contract with no fixed duration. A complex set of case law, resulting in the concept of the "abuse of the right of discharge" de facto grants such workers the guarantee of lifetime employment. Other employees are given fixed duration employment contracts, which generally cannot exceed one year but may be renewed several times over. Other employees also include part-timers, interns, and "dispatched workers" --as workers from temporary work agencies are called in Japan. Until very recently, only a few occupations could be handled by dispatched worker agencies but this is one area where Japanese labor law has in fact been deregulated.

The regulation of private, fee-charging employment agencies – including executive search firms – has also recently been liberalized. Although a fairly time-consuming and bureaucratic licensing procedure is still required, private employment agencies can now serve virtually the entire range of occupations. On-line, Internet based, job seeking and placement services are, however, only in their infancy in Japan – constrained partly by a Ministry of Labor requirement that every employment agency must personally interview each of its clients.

One other anomaly of the Japanese labor market is that there are no defined contribution pension plans. All pension schemes allowed to date are defined benefit plans. Since there is less than complete vesting in most corporate pension plans, this situation serves as an impediment to labor mobility by imposing costs on workers who voluntarily leave their current employer. Legislation now before the Diet would allow the introduction of defined contribution, portable pensions starting in 2001.

E. Foreign-Trade Zones/Free Ports

Japan no longer has any free-trade zones or free ports. Customs authorities, however, do allow the bonding of some warehousing and processing facilities in certain areas adjacent to ports on a case-by-case basis. The GOJ established a law in 1992 entitled the "Law on Extraordinary Measures for the Facilitation of Imports and Foreign Direct Investment in Japan" (effective July 1992 and valid until May 2006). Under the law, the GOJ helps increase access to the Japanese market for foreign goods and capital at government-designated "foreign access zones" near harbors and airports.

F. Capital Outflow Policy

In the 1990's Japan has generally continued to be a net exporter of long term capital, albeit of a lesser magnitude in the late 1980's.

The Japanese Government believes that overseas direct investment will expedite the industrial adjustment of the Japanese economy through its effects of replacing exports and expanding re-imports from Japanese "transplants" overseas.

APPENDIX INVESTMENT STATISTICS

The following tables incorporate JFY99 data for both inward and outward foreign investment in Japan. The data show a drop in U.S. investment in Japan, after the remarkable increase in JFY98. However, total foreign investment in Japan, led by sharp increases by France, the Netherlands and the Cayman Islands, doubled in JFY99, increasing about 400% since JFY97. Japanese investment overseas rebounded as well in JFY99, but the overall ratio of inward FDI remained nearer OECD average levels.

Although the number of cases of U.S. FDI in Japan remained roughly the same as in JFY98, the value was barely half the previous year's total. While there was increased U.S. investment in machinery (by far the largest sector for U.S. investors) and communications, investment in financial services/insurance and services dropped sharply.

The official statistics below represent notification to the Ministry of Finance (MOF) of authorization by MOF of specific planned investment projects (as reported to MOF by companies), not necessarily actual flows of investment. Thus these figures generally exceed by a substantial amount actual investment flows as reported in Japan's balance of payments data. (At the same time, neither the data below nor the balance of payments statistics capture re-investment of profits by foreign firms operating in Japan, or Japanese firms operating overseas. Therefore, according to some academic researchers, both types of official data misstate actual foreign capital investment by a wide margin.)

All data in the tables below is from MOF, current as of June 2000, and converted into dollars using each year's average exchange rate. JF97 data was converted 122.68 yen to the dollar, JFY98 data at 128.02 yen to the dollar, JFY 99 data at 111.54 yen to the dollar.

Table 1: Annual New FDI Into Japan (Billions of Dollars)

JFY	1992	1993	1994	1995	1996	1997	1998	1999
	4.08	3.08	4.16	3.83	6.84	5.53	10.47	21.5

Ratio of Japan's Inward to Outward FDI Flows

JFY	1992	1993	1994	1995	1996	1997	1998	1999
	1:8.4	1:11.7	1:9.9	1:13.4	1:7.02	1:9.77	1:3.9	1:3.1

Table 2: Foreign Direct Investment in Japan, by country

(Million dollars; annual flow; reporting basis)

	JFY 1997	JFY 1998	JFY 1999	Cumulative Total JFY'50-99
N. America	1,240	6,634	3,741	30,745
U.S.	1,237	6,620	2,230	27,506
Canada	2	14	1,512	3,239
Europe	2,509	2,477	12,674	31,154
Neth'lds	1,193	1,049	4,224	10,485
U.K.	364	303	805	3,461
Germany	450	275	419	3,587
Switz.	156	236	344	3,199
France	76	138	6,685	7,765
Asia	605	173	986	986
Singapore	157	60	661	661
Taiwan	40	46	118	118
Hong Kong	333	39	108	1,382
Korea	68	16	95	n/a
L. America	482	281	2,595	n/a
Cayman Isles	430	178	2,257	n/a
BVI	40	11	209	n/a
Bermuda	3	56	56	n/a

Total	5,528	10,985	21,511	n/a

Table 3: Foreign Direct Investment in Japan, by industry

(Million dollars; annual flow; reporting basis)

	JFY 1997	JFY 1998	JFY 1999	Cum. Total JFY 1950-1999
Manufact.	2,180	2,442	8,783	36,425
Machinery	1,184	1,663	7,757	20,950
Chemicals	603	310	541	8,890
Metals	2	16	160	2,144
Rubr/Lthr	153	37	63	1,554
Petroleum	47	66	121	617
Textiles	15	28	2	639
Foods	18	202	13	210
Glass/Cer	6	-	51	171
Other	151	120	76	1,251
Non-manuf.	3,349	8,028	12,727	41,409
Finance/Ins	1,317	3,569	4,586	9,862
Trade	812	1,374	3,124	10,174
Services	724	2,485	1,845	14,098
Real Estate	393	325	151	2,242
Telecom	27	131	2,959	3,441
Transport	3	48	20	287
Construction	2	11	20	141
Other	71	87	22	1,165
Total	5,528	10,470	21,511	77,837

Table 4: U.S. Direct Investment in Japan, by industry
(Note: Data is actually, North America, not U.S.)
(Million dollars; annual flow; reporting basis)

	JFY 1998		JFY 1999	
	$ Amount	# of cases	$ Amount	# of cases
Manufact.	1,300	66	1,711	64
Machinery	1,033	48	1,557	35
chemicals	16	5	26	12
Metals	-	0	30	2
Foods	200	5	5	2

Non-manuf.	5,023	569	2,030	570
Finance/Ins.	2,540	105	543	68
Commerce/Trade	370	167	149	141
Services	1,762	202	961	280
Real Estate	248	61	48	47
Telecom	18	18	312	27
Construction	11	2	11	4
Total	6,323	635	3,741	634

Table 5: Japanese Direct Investment Overseas, by country

(Million dollars; annual flow; reporting basis)

	JFY 1997	JFY1998	JFY 1999	Cum. Total (JFY'50-'99)
N. America	21,395	10,944	24,770	306,038
U.S.	20,774	10,316	22,295	292,469
Canada	620	627	2,474	13,567
Europe	11,207	14,011	25,804	156,848
U.K.	4,120	9,781	11,718	66,342
Netherlands	3,296	2,118	10,360	37,812
Germany	732	553	649	11,116
France	1,736	520	1,127	11,896
Ireland	567	361	460	n/a
Spain	232	122	518	n/a
Asia	12,185	6,528	7,162	126,064
Thailand	1,867	1,371	816	13,882
Indonesia	2,515	1,076	918	25,509
China	1,987	1,065	751	19,521
Singapore	1,824	637	962	15,258
Hong Kong	695	601	971	18,782
Malaysia	791	514	525	9,334
Philippines	523	379	617	5,613
South Korea	443	302	980	7,857
India	434	257	208	n/a
Taiwan	450	224	285	5,932
Vietnam	311	51	99	n/a
L. America	6,338	6,463	7,437	83,710
Cayman Isles	2,539	4,495	2,242	20,232
Panama	1,119	1,040	1,413	28,038
Brazil	1,183	466	654	12,331

BVI	681	177	1,041	n/a
Mexico	320	83	1,484	5,003
Bermuda	195	16	145	4,864
Oceania	2,058	2,213	894	36,129
Australia	1,669	1,387	857	31,257
Africa	332	444	515	9,800
Liberia	161	386	217	7,873
South Africa	131	52	157	n/a
Middle East	471	146	113	5,858
Saudi & Kuwait	132	120	106	901
UAE	196	-	2,890	n/a
Israel	-	5	2	n/a
Total	53,985	40,751	66,694	723,749

Table 6: Japanese Direct Investment Overseas, by industy

(Million dollars; annual flow; reporting basis)

	JFY 1997	JFY1998	JFY 1999	Cumulative Total (JFY '50-'99)
Manufacturing	19,344	12,253	42,310	241,968
Electrical	6,691	3,419	16,350	68,222
Chemicals	3,014	2,247	1,694	30,072
Transport	2,909	1,607	4,781	32,209
Food	572	1,270	14,908	25,704
Metals	1,413	1,223	1,458	21,926
Machinery	1,284	795	995	19,502
Lumber/Pulp	351	677	116	6,215
Textiles	959	341	260	9,392
Other	2,151	673	1,749	28,619
Non-manufacturing	34,067	28,140	24,178	471,812
Finance/Ins.	11,973	16,376	9,885	139,246
Comm/Trade	4,376	3,777	3,877	71,906
Real Estate	5,535	2,810	2,114	93,784
Services	6,480	2,053	4,314	84,837
Transport	2,342	1,898	2,771	37,509
Mining	2,687	874	922	27,358
Construction	456	294	182	5,636
Ag/Forestry	56	33	81	2,451
Fisheries	109	20	26	1,478

Total	53,985	40,751	66,694	723,749

Source: Japanese Ministry of Finance, June 2000

Table 7: Foreign Direct Investment in Japan relative to GDP

	1996	1997	1998	1999
Nominal GDP (a) (trillion yen)	504.4	507.6	487.3	493.8
FDI Inflow (b) (100 billion yen)	7.7	6.8	13.4	24
10 (b/a)	0.15	0.13	0.27	0.49

Source: Japanese Ministry of Finance, June 2000

Restricted Investment Sectors Requiring Prior Notification:

Agriculture
Forestry
Fisheries
Crude Petroleum and Natural Gas Production
Tobacco Manufacturing
Fur Apparel and Apparel Accessories
Miscellaneous Chemical and Allied Products (This sector is unrestricted except for explosives, gelatin, and adhesives.)
Paving materials
Miscellaneous Petroleum and Coal Products. (This sector is unrestricted except for petroleum products.)
Manufacture of Rubber/Plastic Footwear and Accessories
Leather Tanning and Manufacture of Leather Products and Skins
Manufacture of Electrical Generating, Transmission, Distribution, and Industrial Apparatus (This sector is unrestricted except for industries related to aircraft, ordnance, atomic power, and space development.)
Manufacture of Communication Equipment and Related Products. (This sector is unrestricted except for industries related to aircraft, ordnance, atomic power, and space development.)
Ship Building and Repairing, and Manufacture of Marine Engines. (This sector is unrestricted except for industries related to aircraft, ordnance, atomic power, and space development.)
Manufacture of Aircraft and Aircraft Parts
Miscellaneous Transportation Equipment. (This sector is unrestricted except for industries related to aircraft, ordnance, atomic power, and space development.)
Manufacture of Ordnance
Electricity Generation and Distribution

Gas
Heat Supply
Water and Water Supply
Railways, Coastal Transport, and Inland Water Transport
Air Transport
Airplane Services
Ordinary Warehousing (This sector is unrestricted except for industries related to petroleum reserves.)
Communication
Postal Services
Telephone and Telegraph, except Wire Broadcasting Telephone (This sector is unrestricted except for Type I telecommunications business, as defined by Article 6 of the Telecommunications Business Law.)
Services Incidental to Communication (This sector is unrestricted except for telecommunications of Type I carriers in accordance with Article 15 of the Telecommunications Business Law.)
Regional Financial Institutions for Agriculture, Forestry, And Fisheries
Exchanges and Exchange Clearing Houses
Bicycle, Horse, Motorcar, and Motorboat Race Companies
Radio and Television Broadcasting
Guard Services

Designated Technologies Requiring Prior Approval and Technology Import Contracts:

Aircraft
Arms and Explosives Manufacturing
Nuclear Energy
Space Development